

**IN THE
SUPREME COURT OF MISSOURI**

No. 85781

**DIRECTOR OF REVENUE
Appellant,**

v.

**MEDICINE SHOPPE INTERNATIONAL, INC.
Respondent.**

**On Petition for Review from the
Missouri Administrative Hearing Commission
The Honorable Karen A. Winn, Commissioner**

**BRIEF OF RESPONDENT
MEDICINE SHOPPE INTERNATIONAL, INC.**

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JURISDICTIONAL STATEMENT

This appeal involves the construction of a state revenue law. Article V, Section 3 of the Missouri Constitution gives this court exclusive jurisdiction.

STATEMENT OF FACTS

The sole issue, in this case, is whether the interest earned on non operating excess funds invested by Medicine Shoppe International, Inc. (“Medicine Shoppe”) with Cardinal Health, Inc. (“Cardinal Health”) for the tax periods at issue were non Missouri source income under the single factor apportionment provisions of R. S. Mo. § 143.451.2. The decision of the Missouri Administrative Hearing Commission (the “AHC”) found that the interest income received by Medicine Shoppe from Cardinal Health, whose principal office is outside of Missouri was passive investment income that should be excluded from Missouri source income under the single factor apportionment method.

The income tax periods at issue are July 1, 1998 through June 30, 1999 (“1998”); July 1, 1999 through June 30, 2000 (“1999”) and July 1, 2000 through June 30, 2001 (“2000”) (AHC Tr 9). Medicine Shoppe timely filed Missouri corporation income tax returns for each period at issue (within the extended due date).

During the period at issue Medicine Shoppe had an investment agreement (“Investment Agreement”) (AHC Tr 26) with Cardinal Health whereby Cardinal Health invested the excess funds of Medicine Shoppe (AHC Tr 27). Medicine Shoppe had no control over how the funds were invested (AHC Tr 70).

Under the terms of the Investment Agreement, Cardinal Health paid Medicine Shoppe interest on such funds at a rate of return equal to Seven and 72/100 (7.72%) (AHC Tr. Exhibit T) percent per annum.

On its 1998, 1999 and 2000 Missouri income tax returns, Medicine Shoppe calculated its taxable income by using the single factor apportionment method of Section 143.451, R.

S. Mo. Based on the single factor apportionment method, Medicine Shoppe classified and reported its excess passive investment interest income received from its written Investment Agreement with Cardinal Health as non Missouri source income.

The Missouri Director of Revenue (“the Director”) disallowed Medicine Shoppe’s non Missouri source classification for its passive investment interest income from Cardinal Health. The Director’s disallowance resulted in the Director issuing notices of deficiency to Medicine Shoppe for 1998, 1999 and 2000.

Medicine Shoppe timely protested the notices of deficiency for tax years 1998, 1999 and 2000.

Medicine Shoppe timely appealed to the Commission the final decisions described in the previous paragraph to this Commission.

During the tax periods at issue, Medicine Shoppe’s primary business was the franchising of retail pharmacies located throughout the United States. Medicine Shoppe’s income from said business was primarily from (1) origination fees paid by franchisees (also sometimes identified as “licensees”) when the franchises were started; (2) fees from franchisees based on a percentage of the franchisees’ sales; and (3) receipts from the sale of tangible property (pharmaceutical supplies) to the franchisees; and (4) income from loan origination fees; and (5) interest on loans to franchisees.

During the tax periods at issue, Medicine Shoppe also received passive investment interest income from excess working capital funds invested with Cardinal Health. The income at issue in this case does not involve (1) origination fees paid by franchisees (also identified as “licensees”) when the franchises were started; (2) fees from franchisees based

on a percentage of the franchisees' sales; and (3) receipts from the sale of tangible property (pharmaceutical supplies) to the franchisees; and (4) income from loan origination fees; and (5) interest on loans to franchisees.

The income at issue in this case solely involves passive investment interest income received on excess funds invested by Medicine Shoppe with Cardinal Health under the written Investment Agreement.

The issue in this case is entirely different than the issue in the case of *Medicine Shoppe International, Inc. v. Director of Revenue*, 75 S.W. 3d 731 (Mo. banc 2002). None of the interest income involved in this case was part of the previous case. In the previous *Medicine Shoppe* case the AHC and this Court dealt with the issue of whether interest income from loans by *Medicine Shoppe* to its franchisees, outside the State of Missouri, was non Missouri source income under the single factor formula. This Commission and this Court determined that those loans to franchisees were Missouri source income. This Court in the previous *Medicine Shoppe* case held that “there were numerous activities related to the financing of franchising, through the loans provided by Medicine Shoppe, that were conducted from the Company’s St. Louis headquarters. Activities at the St. Louis headquarters included marketing, operations, accounting, finance, advertising, third party contracting, and servicing of franchises.” As noted, four or five Medicine Shoppe employees dealt with credit matters, handling loans to franchisee.” *Medicine Shoppe International v. Director of Revenue*, 75 S.W.3d 731, 734 (Mo. banc 2002). The interest income from loans to franchisees is not an issue on this case.

This case involves only one item of income and that is passive investment interest income received by Medicine Shoppe on excess funds invested with Cardinal Health.

POINT RELIED ON

The Administrative Hearing Commission did not err in finding that the funds Invested by Medicine Shoppe International, Inc., with its parent corporation, Cardinal Health, Inc. are non-Missouri source income under the Single Factor Apportionment Formula under Section 143.451 R. S. Mo.

STANDARD OF REVIEW

This Court must uphold the AHC's decision if it was authorized by law and supported by competent and substantial evidence upon the entire record, and if it is not clearly contrary to the reasonable expectations of the General Assembly. *Jones v. Director of Revenue*, 981 S.W.2d 571, 574 (Mo. banc 1998). *Buchholz Mortuaries, Inc. v. Director of Revenue*, 1135 S.W.3d 192, 193 (Mo. banc 2003). Under this standard, this Court essentially adopts the AHC's factual findings. *Concord Publishing House v. Director of Revenue*, 916 S.W.2d 186, 189 (Mo. banc 1996).

ARGUMENT

The Administrative Hearing Commission Did Not Err In Finding That The Funds Invested By Medicine Shoppe International, Inc., With Its Parent Corporation, Cardinal Health, Inc. Are Non-Missouri Source Income Under The Single Factor Apportionment Formula Under Section 143.451 R. S. Mo.

In *Petition of Union Electric Company of Missouri*, 161 S.W.2d 968 (Mo. 1942) (hereinafter cited as “*Union Electric*”) and *Union Electric Company v. Coale*, 146 S.W.2d 631 (Mo. 1940) (hereinafter cited as “*Coale*”), this Court held that income derived from a loan of money to a non Missouri resident borrower for use wholly outside of Missouri was not Missouri source income under the single factor method of apportionment set forth in Section 143.451. This Court in *Medicine Shoppe International, Inc. v. Director of Revenue*, 75 S.W. 3d 731 (Mo. banc 2002) affirmed the *Union Electric* findings stating that “The Union Electric cases retain vitality to the extent that they recognize that wholly passive investments outside the state of Missouri are not included in the taxation formula used to determine Missouri taxable income . . .”

The Missouri Administrative Hearing Commission found as a matter of fact: that the interest in question was passive income. It is from an activity in which Medicine Shoppe does not materially participate. The interest is similar to that at issue in cases such as the *Union Electric* cases, which Medicine Shoppe noted retained some vitality. (AHC Decision at P29).

The case of *Acme Royalty Company v. Director of Revenue* 965 S.W. 3d 72 (Mo banc 2002) did not alter or change the rule that has existed since *Union Electric*. Section 143.451

still states that a corporation can have non-Missouri source income. The issue of “no where income” is irrelevant. The issue is what has the legislature seen fit to tax. Section 143.451 still states that Missouri taxable income of a corporation shall include all income derived from sources within this state.

Acme Royalty Company dealt with payments of exclusive licensing agreements and patents between corporate taxpayers which this court determined that payments resulting from exclusive licensing agreements and patents between corporate taxpayers and related companies were not sales in Missouri attributable to *Acme Royalty Company*.

Under Appellant’s theory a Missouri company could not, under any circumstances, have non-Missouri source income. This concept is directly contrary to the statutory language of §143.451. This court in *Acme* specifically states “the seminal rule of statutory construction directs this Court to determine the true intent of the legislature, giving reasonable interpretation in light of the legislature objective. Taxing statutes in particular are to be strictly construed in favor of the taxpayer and against the taxing authority when any ambiguity exists.

This Court has also held that tax “is purely a matter of statute and within the power of the legislature, subject to constitutional limits, *International Business Machines v. Director of Revenue* 958 S.W. 2d 554 (Mo banc 1998). See also *City of St. Louis v. Carroll*, 494 S.W. 2d 1 (Mo 1973).

The legislature has chosen not to change this language and clearly intended for there to be non- Missouri source income.

I. A Corporation under the statutory Single Factor Formula is only required to pay tax on Missouri source income.

Missouri law allows a corporation doing business within and without Missouri alternative methods to allocate and apportion its income for Missouri income taxation. First, a corporation may elect to use the single factor apportionment method of Section 143.451. Alternatively, a corporation may elect to use the Multistate Tax Compact (“MTC”) formula under Section 32.200 to apportion its business income based upon the three factor formula averaging property, payroll and sales ratios to derive its Missouri taxable income. Under that formula, non-business income is allocated under special rules. *See Philip Morris, Inc. v. Director of Revenue*, 760 S.W.2d 888, 889 (Mo. banc 1988); *Luhr Bros., Inc. v. Director of Revenue*, 780 S.W.2d 55, 57 (Mo. banc 1989). The MTC formula reflects a test of entitlement to allocation and apportionment on whether the taxpayer is taxable in another state. The MTC formula has been in effect since 1967. The Single Factor Formula and MTC Formula are totally separate and unique apportionment formulas. The Director wrongfully assumes that corporations are required to pay tax on all income derived from Missouri and non-Missouri sources and that the separate apportionment formulas are simply alternative accounting methods that should reach the same result.

There is no dispute that Medicine Shoppe timely elected the single factor apportionment method under Section 143.451. Likewise, single factor apportionment under Section 143.451 does not embrace the distinction between business and non business income that the Compact emphasizes. In *Dow Chemical Company v. Director of Revenue*, 787 S.W.2d 276, 284 (Mo. banc 1990), the Court discussed the differences between the two

apportionment methods. The Court concluded that the source of income test and its single factor method of apportionment were a complete and integrated system of apportionment, separate and apart from the MTC formula designation of business and nonbusiness income and its three factor apportionment formula. *Id.*; In *Goldberg v. State Tax Commission*, 639 S.W.2d 796 (Mo. banc 1982) the Court reaffirmed the long standing judicial interpretation of Section 143.451 as proper in determining issues regarding the source of income under the single factor method of apportionment. The MTC formula apportions income on the premise that a multi state corporation operates as a unitary business. Under the single factor apportionment method, on the other hand, unitary concepts are irrelevant, and the focus is upon what Missouri has characterized as the “source of income” taxation. *Dow Chemical Company, Inc. v. Director of Revenue*, 834 S.W.2d 742 (en banc, 1992).

II. “Single Factor” Apportionment Does Not Include Certain Income Which is Non-Missouri Source Income.

A. Missouri Taxable Income

Section 143.451, R. S. Mo., states:

1. Missouri taxable income of a corporation shall include all income derived from sources within this state.
2. A corporation described in subdivision (1) of subsection 1 of section 143.441 shall include in its Missouri taxable income all income from sources within this state, including that from the transaction of business in this state and that from the transaction of business partly done in this state and partly done in another state or states.

The statutory language is clear that only income from sources entirely within or partially within Missouri is subject to Missouri corporate income taxation. The statute is clear and unambiguous on its face. The Missouri Supreme Court in *Wolff Shoe Company v. Director of Revenue*, Missouri Supreme Court, 762 S.W.2d 29 (1988) stated:

The primary rule of statutory construction is to ascertain the intent of the legislature from the language used, to give effect to that intent if possible, and to consider the words used in their plain and ordinary meaning. *Metro Auto Auction v. Director of Revenue*, 707 S.W.2d 397, 401 (Mo. banc 1986). And, where a statute's language is clear and unambiguous, there is no room for construction. *Id.* In determining whether the language is clear and unambiguous, the standard is whether the state's terms are plain and clear to one of ordinary intelligence. *Alheim v. F.W. Mullendore*, 714 S.W.2d 173, 176 (Mo. App. 1986). Moreover, the plain and unambiguous language of a statute cannot be made ambiguous by administrative interpretation and thereby given a meaning which is different from that expressed in a statute's clear and unambiguous language. *Blue Springs Bowl v. Spalding*, 551 S.W.2d 596, 600 (Mo. banc 1977).

The "Source of Income" test focuses upon what Missouri law has characterized as "source of income" taxation. *Dow Chemical Co. v. Director of Revenue*, State of Missouri (1990, Mo. S. Ct.) 787 S.W.2d 276. The Source of Income has been defined as the place where the income was produced. *In Re Kansas City Star Company*, 142 S.W.2d 1029 (en banc 1940). See also *Bass Pro Shops, Inc. v. Director of Revenue* 746 S.W.2d 97 (en banc

1988). Under the source of income concept, it is well established that income produced or sourced outside Missouri is excludable from income subject to Missouri taxation. *Dow Chemical Company, Inc. v. Director of Revenue*, 1989 WL 103255 (Mo banc 1989).

With respect to dividend income, this Court noted that the actual use of the capital that gave rise to the income represented by the dividends took place outside Missouri. In *Union Electric* the Court concluded that “[the source of income is the place where it was produced[.]” *Id.* at 635. In *Petition of Union Elec. Co. of Missouri*, 161 S.W.2d 968, 970 (Mo. banc 1942), the Court reexamined the facts presented in the previous *Union Electric* case (*Union Electric Co. v. Coale*, 146 S.W.2d 631 (Mo. 1940)). In *Petition of Union Electric Co. of Missouri*, this Court dealt with the issue of interest on bonds issued by the Union Electric Company of Illinois but held by the taxpayer in Missouri. The taxpayer excluded these items from Missouri taxable income as non Missouri source income. The payors of the interest and dividends were located in Illinois, the obligation was not secured by any liens on Missouri property, and the capital was utilized in Illinois. The Court held that the entire amount of interest income was non Missouri source income properly excluded by taxpayer from its Missouri income subject to apportionment. In addition the Court found that the actual expenditure of labor and the use of capital which gave rise to the income took place outside the state of Missouri. The issue presented was whether or not the dividends and interest payments are income received by the taxpayer from sources within this state. This Court held that the focus of the source of income is determined as follows: In the case of income derived from labor, it is the place where the labor is performed; in the case of income derived from use of capital, it is the place where the capital is employed; and in the

case of profits from the sale or exchange of capital assets, it is the place where the sale occurs. The *Acme Royalty* case has not abrogated the single factor non-Missouri source of income test.

B. Passive Investment Interest Income Is Not Missouri Source Income

In *Goldberg v. State Tax Commission*, 639 S.W.2d 796 (Mo. 1982), the Court affirmed the source of income test. Clearly the legislature and the Court has recognized that Missouri headquartered companies can and do have non Missouri source income. The company in *Goldberg* was a Missouri corporate manufacturer, located in Missouri and it neither owned property nor maintained branch offices outside Missouri. It had elected the single factor method and it paid no income tax to any state other than Missouri. The issue in *Goldberg* was whether the company, for purposes of determining its Missouri income tax liability, should apportion the income it derived from the sale of goods to out of state customers. The Court in *Goldberg* stated that at the time Missouri adopted the MTC in 1967 the “source of income” test embodied in present § 143.451 was effective and therefore was recognized as controlling under Article III, §1 of the Compact” and the legislature could have provided in adopting the Compact to eliminate the source of income test. However, the *Goldberg* Court stated that “It is clear, therefore, that the legislature did not intend by the adoption of the Compact to vitiate the ‘source of income’ test of § 143.451.” *Id.* The Missouri legislature has never repealed the source of income test in Section 143.451.1. The legislature has had many opportunities to amend the income tax statutes. The legislature could have easily have amended the statutory language to eliminate the source of income test when Missouri adopted the MTC.

In this matter Medicine Shoppe derived passive investment interest income by investing its excess funds with Cardinal Health. Medicine Shoppe elected to use the single factor method of apportionment under Section 143.451. Therefore, Medicine Shoppe's passive investment interest income, earned outside the State of Missouri, should not be treated as Missouri source income.

The Court has consistently followed its holding in *Petition of Union Electric* that income earned from the use of capital outside of Missouri is not Missouri source income, and therefore not subject to apportionment under the single factor method of Section 143.451. *See, e.g., Union Electric Company v. Coale*, 146 S.W.2d 631 (Mo. 1940) (dividend income received from companies operating exclusively outside Missouri was not Missouri source income); *A.P. Green Fire Brick Company v. State Tax Commission*, 277 S.W.2d 544 (Mo. 1955) (royalty income paid by foreign corporation for use of Missouri corporation's trademarks, trade names and manufacturing processes is not Missouri source income and not subject to single factor apportionment because income was derived from activities outside Missouri); *Brown Group, Inc. v. Administrative Hearing Commission*, 649 S.W.2d 874 (Mo. banc 1983) (royalty income earned by Missouri corporation for use of Missouri corporation's trade names, shoe designs and shoe patterns is not Missouri source income and not subject to single factor apportionment because income was derived from activities outside Missouri).

Medicine Shoppe's passive investment interest income was derived solely through the use of this capital outside of Missouri. Therefore, under this Court's long standing interpretations of the source of income rules, Medicine Shoppe's passive investment interest income is not Missouri source income subject to tax under Section 143.451.

C. **Passive Investment Income**

Passive investment income is not defined in Chapter 143 R. S. Mo. However, the common use of passive investment income is the definition found in the Internal Revenue Code “gross receipts derived from royalties, rents, dividends, interest, annuities and sales or exchanges of stock or securities.” (I.R.C. 1362(d)(3)(C)(i)). The Missouri Department of Revenue has included in its General Definitions for Regulation 12 Mo. Code of State Regulations 10 2.210 (Income Tax-Airlines) a reference to “passive income.” The regulation states “passive income items such as interest, rental income, dividends and the like . . .

In *Maxland Development Corporation v. Director of Revenue*, 960 S.W.2d 503 (Mo. banc 1998) this Court dealt with passive income. The *Maxland* case actually involved three appeals in which a corporation headquartered in Missouri owned a fractional interest in a shopping center located outside of Missouri. In two of the cases, this Court held that the use of labor from the Missouri headquarters for managing the corporation’s interest in the shopping center made all such income derived from sources partly within and partly without Missouri. *Id.* at 506. In the third case, the one involving a Michigan shopping center, the corporation owned its interest as a triple net lease, whereby the lessee paid all of the expenses, including maintenance, insurance, taxes and utilities. Because this corporation was not expending labor in producing its income under the triple net lease, this Court held that this income was not Missouri source income. *Id.* at 507.

The Administrative Hearing Commission found as a matter of fact that the investment by Medicine Shoppe with Cardinal Health was passive:

the interest income at issue in this case fits within the definitions of passive income as set forth in 26 U.S.C. §469 and 26 U.S.C. §1362(d)(3)(C). The income is interest income from an activity in which Medicine Shoppe does not materially participate. Medicine Shoppe's management in Missouri has no control over production of the investment income...

This Court has held that the *Union Electric* cases retain vitality to the extent that they recognize that wholly passive investments outside the state of Missouri are not included in the taxation formula used to determine Missouri taxable income. Medicine Shoppe's interest earned on non-operating excess funds invested by with Cardinal Health, Inc. is passive investment income and should be excluded from the single factor formula as non-Missouri source income.

III. The Court Should Not Overrule *Brown Group* Since It Does Not Depart From the Statutory Language Duly Enacted By The Missouri Legislature.

The Missouri Supreme Court in *Brown Group* dealt with royalties paid by a foreign corporation, the source of which was wholly outside of Missouri, as the trade names and manufacturing processes involved were used and income produced in Japan and other foreign countries to which the Japanese payor exported shoes. The Missouri Supreme Court held that the royalties did not figure in the taxing formula applicable to payee corporation, which had its principal place of business in Missouri, and thus were properly excluded from the multiplicand (the net income) to which the single factor formula applied.

One of the specific issues the Missouri Supreme Court decided in *Brown Group* was the same issue the Appellant raises which is whether non-Missouri source income “may be excluded from the multiplicand of the single factor formula” . . . in *Brown Group* this Court held:

Petitioner’s third point involves the inclusion of royalties from a corporation of a foreign nation in the multiplicand of the single factor formula. The Director argues that when a taxpayer elects under § 143.451.2(2) to apportion income using the single factor formula it is precluded from allocating any of its income prior to apportionment and that the legislature intended to levy and apportion tax upon the entire net income. The Petitioner counters that income from sources wholly outside Missouri is not taxable . . . This Court, in construing the predecessor of § 143.451, has held that subsection 1 of § 143.040, R. S. Mo. 1969 actually imposed the tax while subsection 2 of the statute dealt only

with how to compute the tax levied in subsection 1. *International Travel Advisors, Inc. v. State Tax Commission*, 567 S.W.2d 650, 654 (Mo. banc 1978). So too, in subsection 1 of § 143.451, a tax is imposed which includes all income derived from sources within this state. Therefore, the Director's argument that § 143.451.2(2)(b) extends to tax income from all sources because it uses the term "net income" without qualification cannot be accepted in light of those provisions which restrict taxation of a corporation's income to that derived from sources within this state. See §§ 143.431 and 143.451.1. (Emphasis added)

This Court, in *Brown Group*, further stated:

Director's offered distinction cannot overcome the language of §§ 143.431.1 and 143.451.1, the present taxing statutes, which define Missouri taxable income as so much of a corporation's federal income tax as is derived from "sources within Missouri." This clear statement of legislative intent is not enervated in any regard by the language of § 143.451.2(2)(b) indicating that "net income" is to be multiplied by the fraction obtained pursuant to that section. We hold fast to the basic precept that tax statutes are to be strictly construed in favor of the taxpayer and against the taxing authority. *Staley v. Missouri Director of Revenue*, 623 S.W.2d 246, 250 (Mo. banc 1981). The Director's argument that upon election by the taxpayer to use the single factor formula, all income from any source must be included in the base income is out of phase with that principle. Accordingly, the Administrative Hearing

Commission's decision is reversed with respect to the propriety of including the foreign royalties in petitioner's net income base under the single factor formula for the 1973-75 tax years (emphasis added).

The Director of Revenue is attempting to revise legislation through this Court. The *Brown Group* case was decided in 1983. There have been twenty (20) legislative sessions since that case and the legislature has seen fit to not change the language of § 143.451. As previously stated, the statutory language is clear and unambiguous on its face. If it was the intent of the legislature to have this statute interpreted differently, it has had ample time in 20 years to do so. In addition the MTC formula has been in place since 1967. Again the legislature has not seen fit to alter or eliminate the single factor formula or the Missouri source language in §143.451. The legislative intent is clear that there is non-Missouri source income.

The revision to Section 143.451 has also been an issue in the last two legislative sessions. Again, the legislature saw fit not to change the statute.

Respondent, in its reply brief filed at the Missouri Administrative Hearing Commission requested that the Commission take judicial notice of the following:

A. Governor Holden's State of the State Address dated January 15, 2003. In this speech in reference to loopholes, the Governor states "Another Missouri tax loophole exempts royalties, dividends, and interest income Missouri business receive from their out-of-state interests."

B. Senate Bill 536 (which did not become law) of the 92nd General Assembly (2003 session) proposed the following changes to Section 143.451, R. S. Mo.:

1. Missouri taxable income of a corporation shall include all income ~~derived from sources within this state~~² **as apportioned pursuant to this section**³. . .

2. A corporation described in subdivision (1) of subsection 1 of section 143.441 shall include in its Missouri taxable income all income ~~from sources within this state~~, including that from the transaction of business in this state and that from the transaction of business partly done in this state and partly done in another state or states . .

. (2) The taxpayer may elect to ~~compute the portion of~~ **apportion** income from all sources in this state **to Missouri** in the following manner: (a) ~~The~~ **All federal taxable income** (from all sources) **for the taxable year with the modifications specified in subsection 2 and 3 of section 143.431** shall be determined as provided, excluding therefrom the figures for the operation of any bridge connecting this state with another state . . .

C. Senate Bill 687 (which did not become law) of the 92nd General Assembly (2003 session) proposed making the same changes to Section 143.451 as Senate Bill 536.

D. House Bill No. 503 (which did not become law) of the 92nd General Assembly (2003 session) proposed making the same changes to Section 143.451 as Senate Bill 536.

E. The Missouri Department of Revenue “Corporation Allocation and Apportionment of Income” tax forms (MO-MS) state; under Part A “Missouri Taxable Income – Missouri Sources”, under Part B, Line 3 “Amount of sales wholly without Missouri,” under Part B line 9 “Non-Missouri source income” and Part C line 7 “Non-Missouri source income (single factor).” The position that nothing in the language of the

² Strikeout language is the language proposed to be eliminated by Senate Bill 536.

³ Bold language is the language proposed to be inserted by Senate Bill 536.

statute suggests a category of income that is excluded from net income (*i.e.*, allocated outside Missouri as “non-Missouri source” income) before the net income is multiplied by the apportionment factor is inconsistent with the Department of Revenue’s own tax forms.

The one thing all of the above proposed legislation and Governor Holden’s statements have in common is that they all attempt to fix a problem that the Appellant states does not exist. In addition, the Department of Revenue’s forms clearly indicate that there is an item of non-Missouri source income.

The *Brown* case is clearly consistent with the statutory framework in Section 143.451 and should not be overruled.

CONCLUSION

Section 143.451 R. S. Mo. is a taxing statute, so that Section 136.300 R. S. Mo. requires:

any issue relevant to ascertaining the tax liability of a taxpayer all laws of the state imposing a tax shall be strictly construed against the taxing authority in favor of the taxpayer.

The Medicine Shoppe correctly excluded the passive investment interest income from non Missouri investments as non-Missouri income. In addition, the Director of Revenue’s disallowance, as non-Missouri source income, is inconsistent with Section 143.451, R. S. Mo. and the case law thereunder.

Accordingly, we respectfully request that this Court affirm the decision of the Missouri Administrative Hearing Commission.

Respectfully submitted,

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ATTORNEYS FOR RESPONDENT

**CERTIFICATION OF SERVICE AND
OF COMPLIANCE WITH RULE 84.06(B) AND (C)**

The undersigned hereby certifies that on this 20th day of July, 2004, two true and correct copies of the foregoing brief, and one disk containing the foregoing brief, were mailed, overnight mail, postage prepaid, to:

James R. Layton
State Solicitor
P.O. Box 899
Jefferson City, Missouri 65102

The undersigned certifies that the foregoing brief complies with the limitations contained in Rule No. 84.06(b), and that the brief contains 5,726 words.

The undersigned further certifies that the labeled disk, simultaneously filed with the hard copies of the brief, has been scanned for viruses and is virus-free.

RICHARD E. LENZA